



Onshore and offshore bonds

Are they back or have they never been away?

The information that follows is based on our understanding of current taxation, legislation and HM Revenue & Customs practice all of which are liable to change without notice.

This is just for UK advisers – it's not for use with clients

This content is based on our understanding of current taxation, legislation and HM Revenue & Customs practice all of which are liable to change without notice. The impact of any taxation (and any tax reliefs) depends on individual circumstances.

Where content includes case studies or examples these are for illustration purposes and are not recommending a specific course of action.

Past performance is not a reliable indicator of future performance. The value of an investment can go down as well as up and your client may get back less than they've paid in.

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Learning Objectives

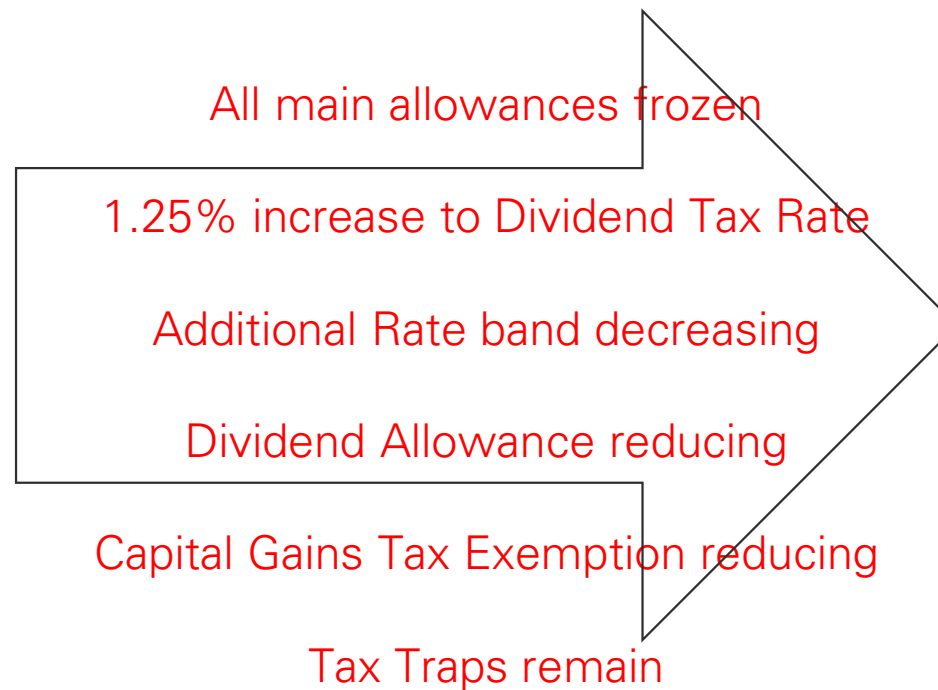
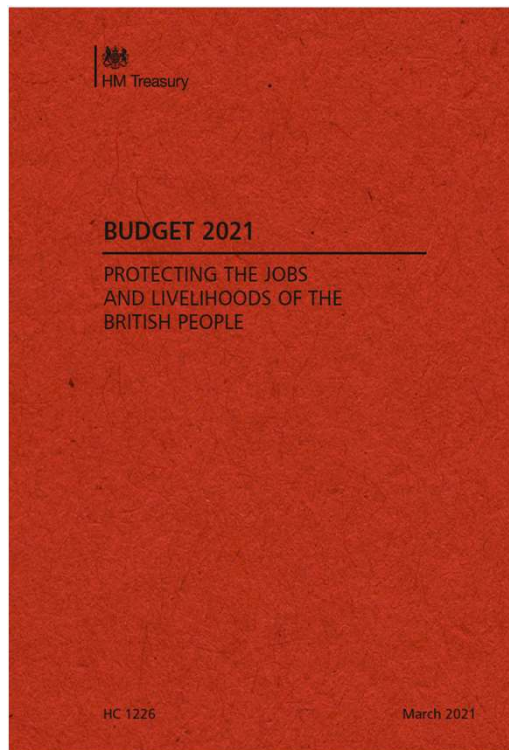
By the end of this session, you will be able to:

Describe the impact of the changing tax landscape on investment advice

Describe the taxation of insurance bonds

Identify clients who would benefit from using insurance bond wrappers

So, where are we...



3.2 million new taxpayers

2.6 million new higher rate taxpayers

232,000 new additional rate taxpayers

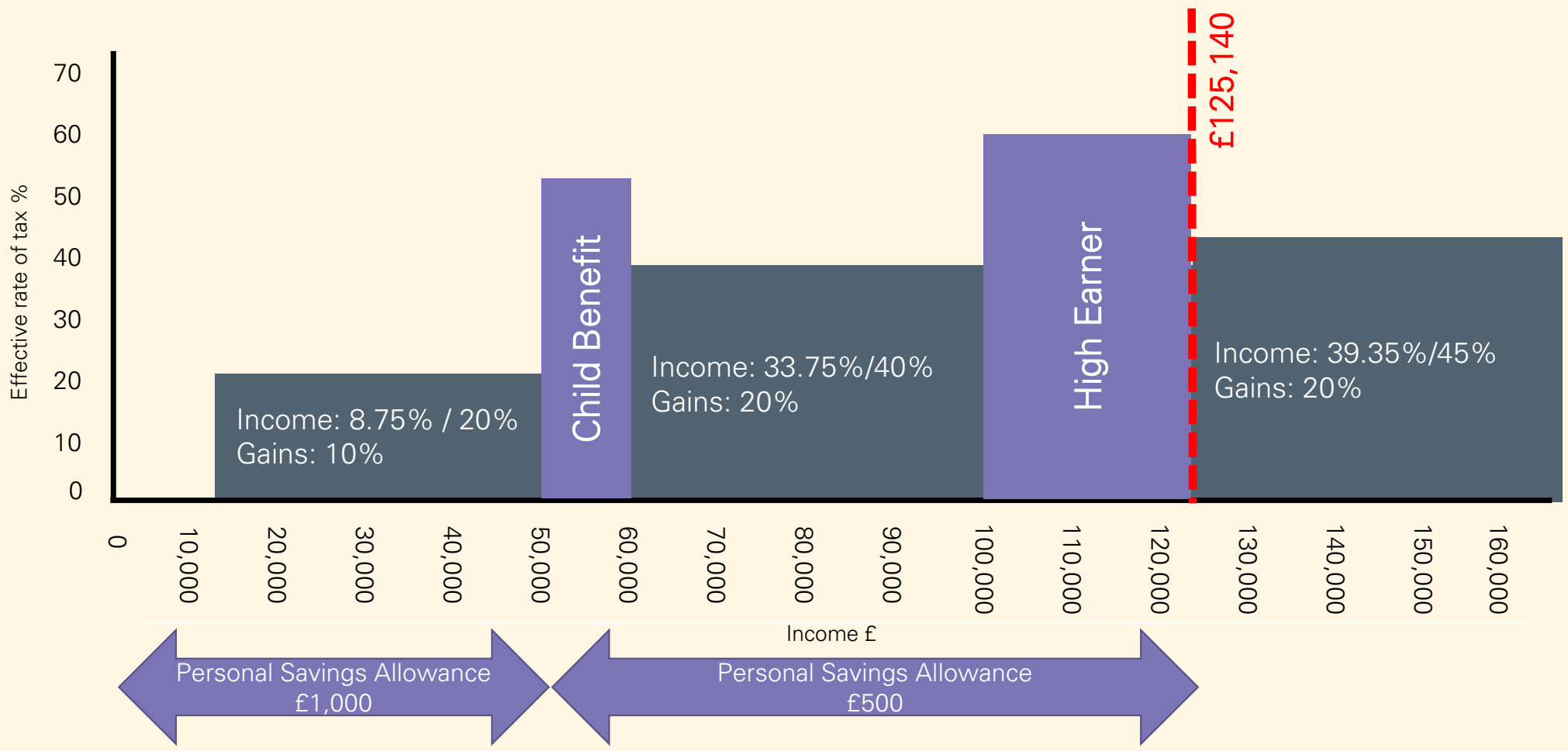
c1.5m to 3m new dividend taxpayers

260,000 new Capital Gains Taxpayers

Ever Increasing IHT receipt




UK Income Tax Landscape



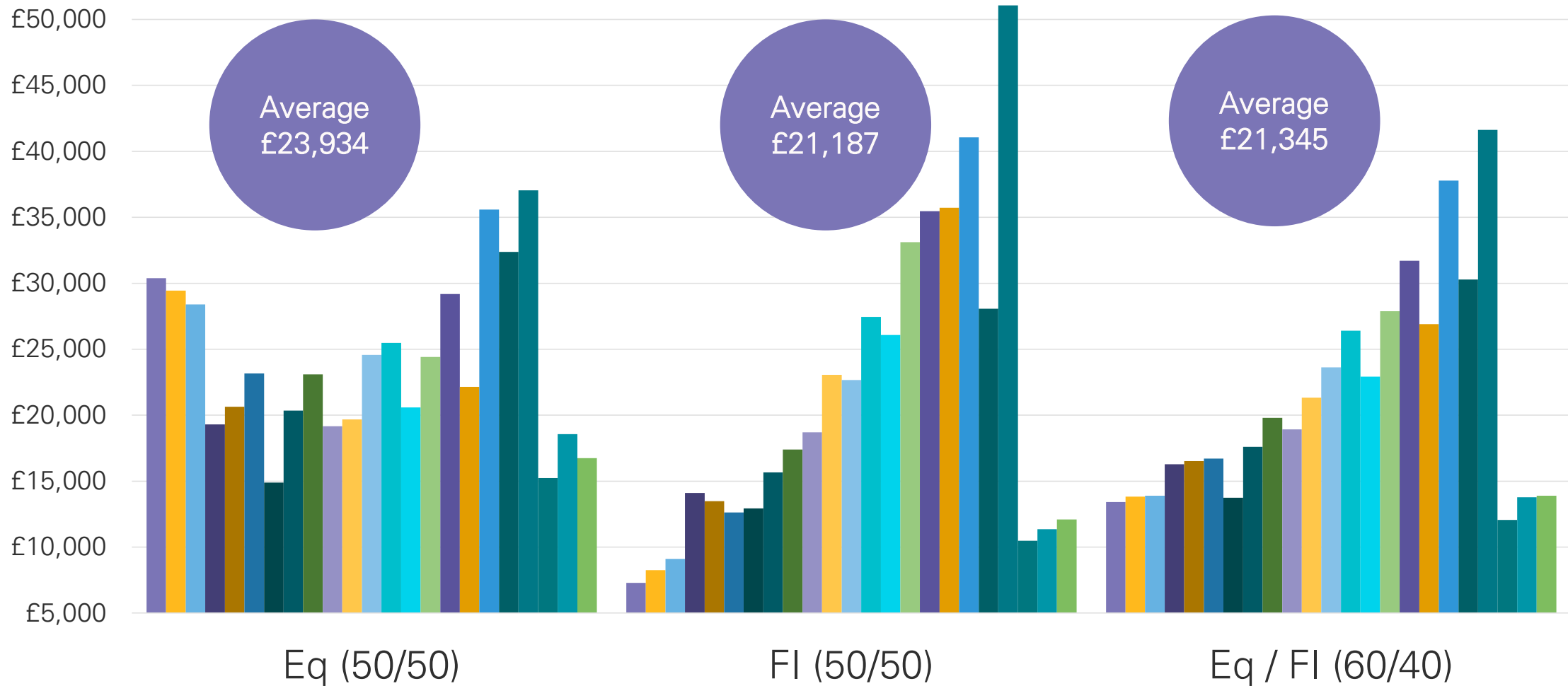
The full amount of bond gains and interest and dividends are included at Step 1 of the UK income tax computation.

0%_s

	2022/23	2023/24	2024/25
ANNUAL EXEMPT AMOUNT Capital gains only	£12,300	£6,000	£3,000
DIVIDEND NIL RATE Dividends only	£2,000	£1,000	£500
SAVINGS STARTING RATE / PERSONAL SAVINGS ALLOWANCE Interest and Bond Gains	£5,000 £1,000 / £500	£5,000 £1,000 / £500	£5,000 £1,000 / £500
PERSONAL ALLOWANCE Interest, Dividends and Bond Gains	£12,570	£12,570	£12,570
	£32,870 + Original Capital	£25,570 + Original Capital	£22,070 + Original Capital



Fund to generate £500 income (2000 - 2022)



Income received as a % total profit

Period	UK Equity	Global Equity	Equity (50/50)	UK Fixed Interest	Global Fixed Interest	Fixed Interest (50/50)	Mixed (30/30/20/20)
2000 - 2022	45%	21%	69%	49%	30%	57%	40%
2000 – 2009	150%	804%	93%	64%	220%	76%	100%
2007 – 2016	50%	23%	65%	42%	32%	51%	39%
2013 - 2022	51%	19%	172%	81%	28%	110%	40%

£100,000 invested, Year ending 31/12, Gross income reinvested

Selling down £20,000 a year

- £100,000 invested,
- Capital Return only,
- 19 periods starting 2000,
- AEA at £3,000

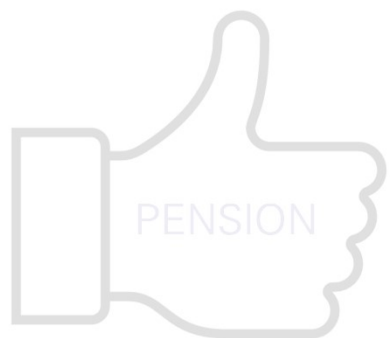
	Equity (50/50)		Fixed Interest (50/50)		Mixed Investment 30/30/20/20	
	Years until ISA		Years until ISA		Years until ISA	
	wrap complete	Taxable Gains	wrap complete	Taxable Gains	wrap complete	Taxable Gains
2000	4	0	6	0	5	0
2001	4	0	6	0	5	0
2002	5	0	5	0	5	0
2003	7	6	5	0	7	3
2004	7	4	5	0	6	2
2005	6	3	5	0	6	0
2006	6	0	5	0	5	0
2007	5	0	6	0	5	0
2008	5	0	6	0	5	0
2009	6	0	6	0	7	0
2010	6	0	6	0	6	3
2011	6	2	6	0	6	0
2012	8	6	6	0	7	5
2013	8	6	6	0	7	3
2014	7	4	6	0	6	4
2015	7	5	6	0	6	3
2016	7	5	6	1	7	4
2017	6	0	5	0	6	0
2018	5	0	5	0	5	0

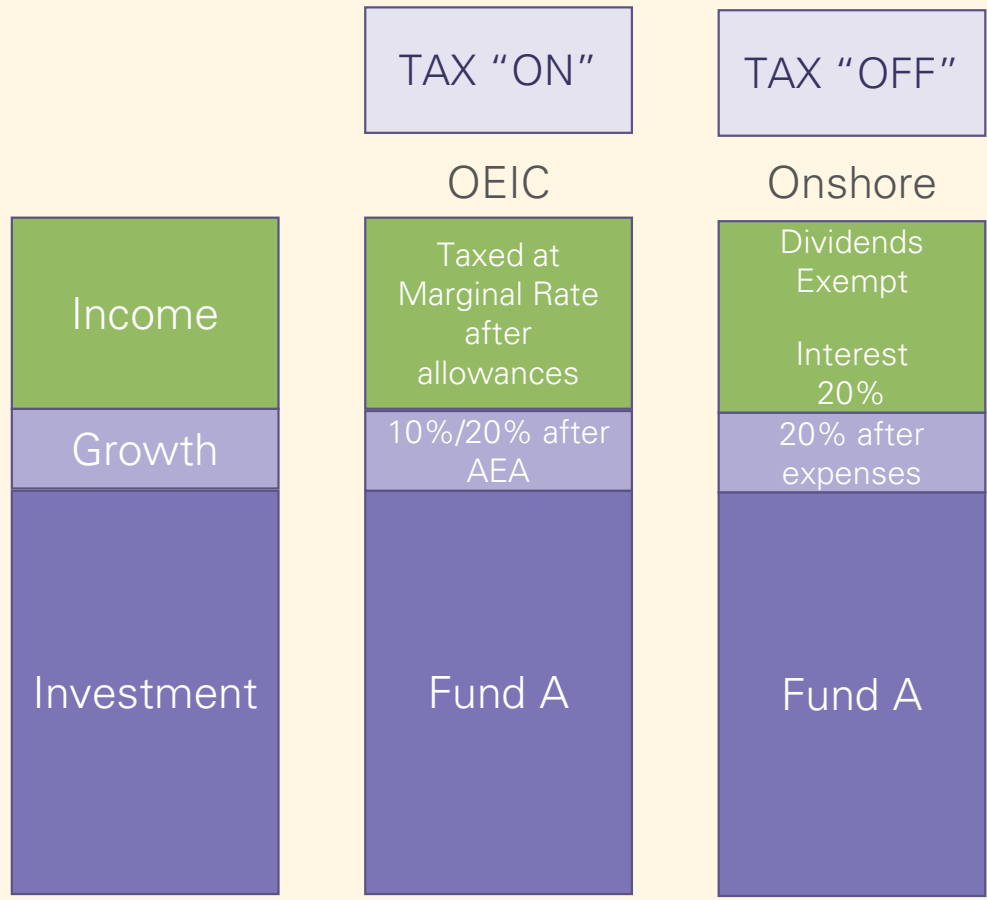
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9

“Wrappers”



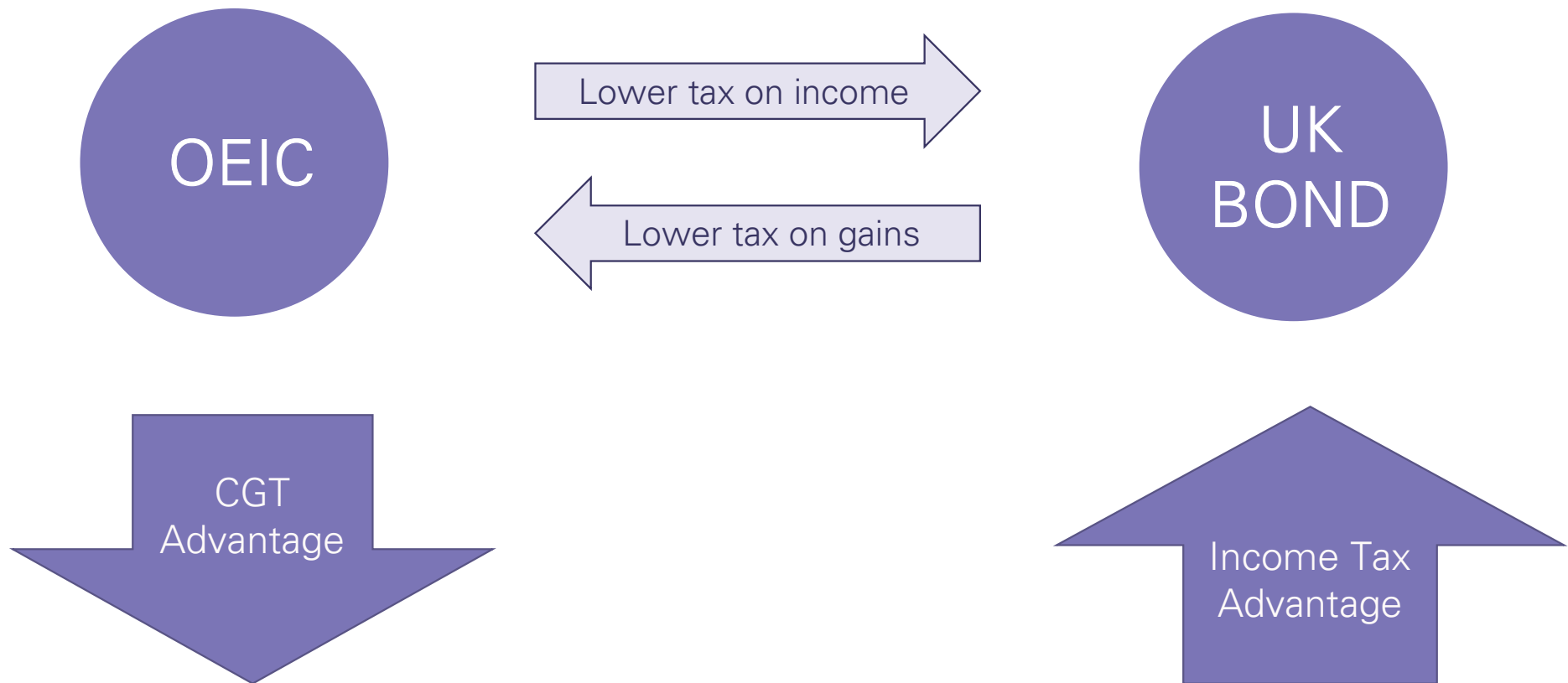


OEIC – to wrap or not to wrap

			Unwrapped	UK Bond Wrapped
	Yield	Amount	Tax	
Dividend	3%	£3,000	£1,012	£0
Income	1%	£1,000	£400	£200
Gain	2%	£2,000	£0	£400
Total	6%	£6,000	£1,412	£600
		Effective rate	23.5%	10%

£100,000 invested, higher rate taxpayer, AEA £3,000, income above savings or dividend allowance

The trade off

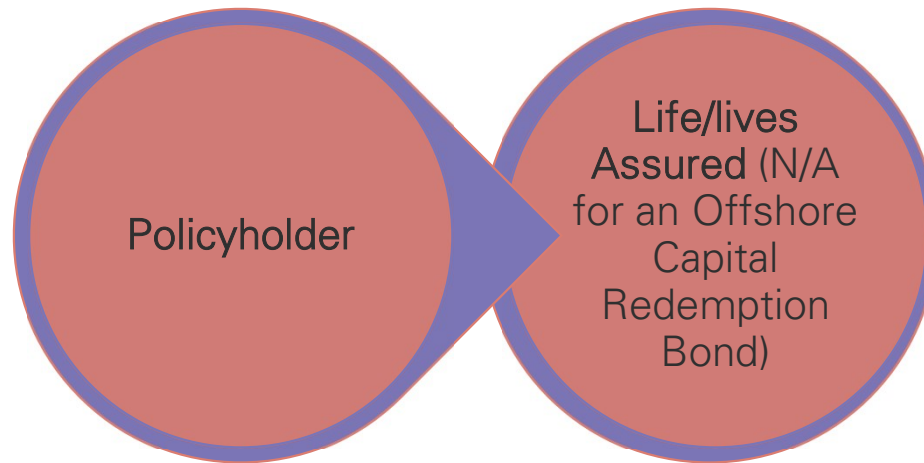


First things first

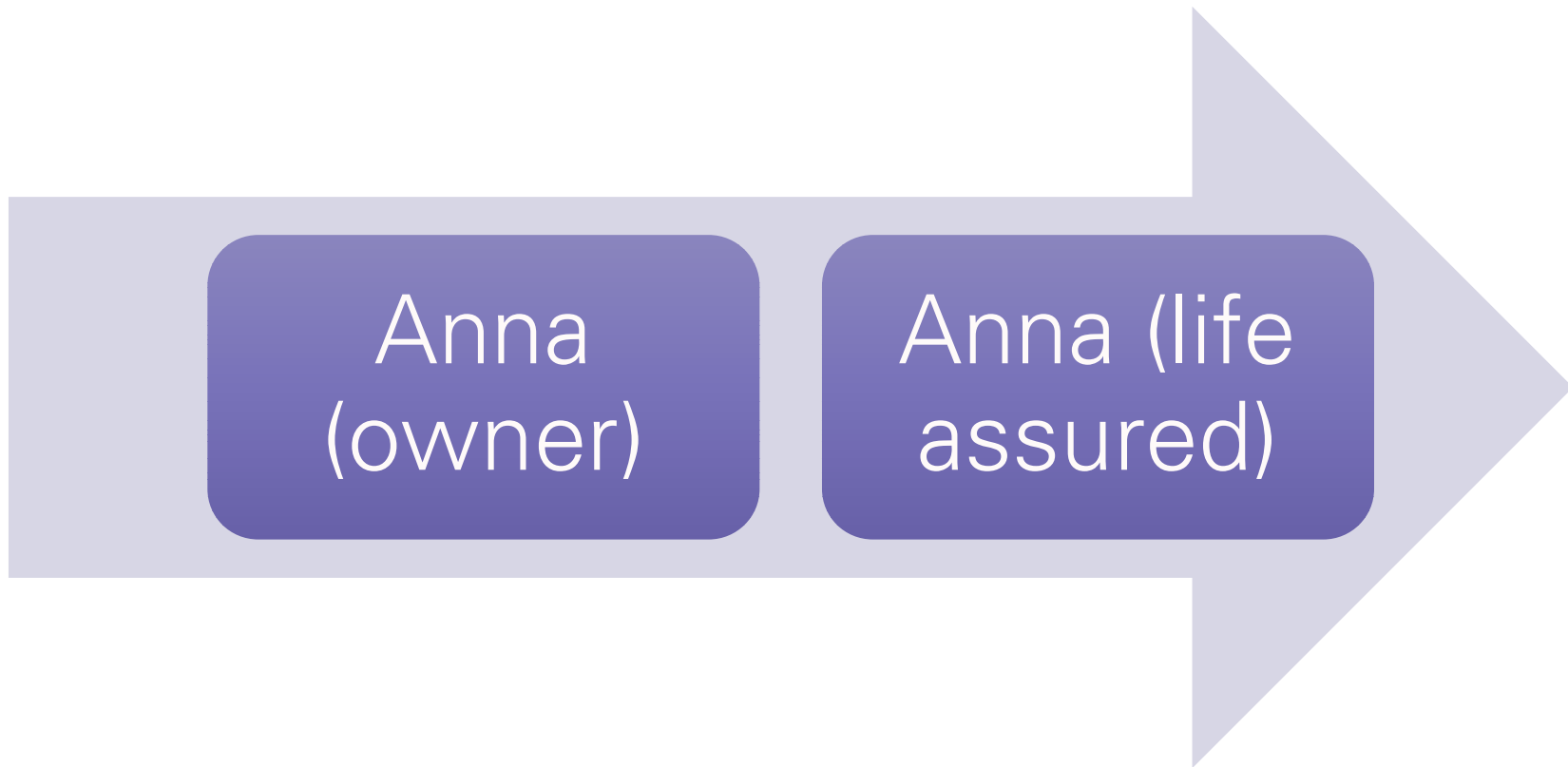
Describing a bond to a client

- non-qualifying,
- single premium,
- whole of life assurance or capital redemption policy

Setting up a Bond since 1774 (can be confusing for clients)



Insurable interest – own life policy



Insurable interest – additional life assured



Anna (owner)

Lives assured are
Anna & Bert
(Anna's husband)

Insurable interest – life of another policy

Alphabet Ltd
(company owner)

The diagram consists of a large, light blue arrow pointing to the right. Inside the arrow, there are two rounded rectangular boxes. The left box is dark blue and contains the text 'Alphabet Ltd (company owner)'. The right box is a lighter shade of blue and contains the text 'Life assured is Director (Mr A)'. The arrow's tail is on the left and its head is on the right, indicating a flow or relationship from the company owner to the life assured.

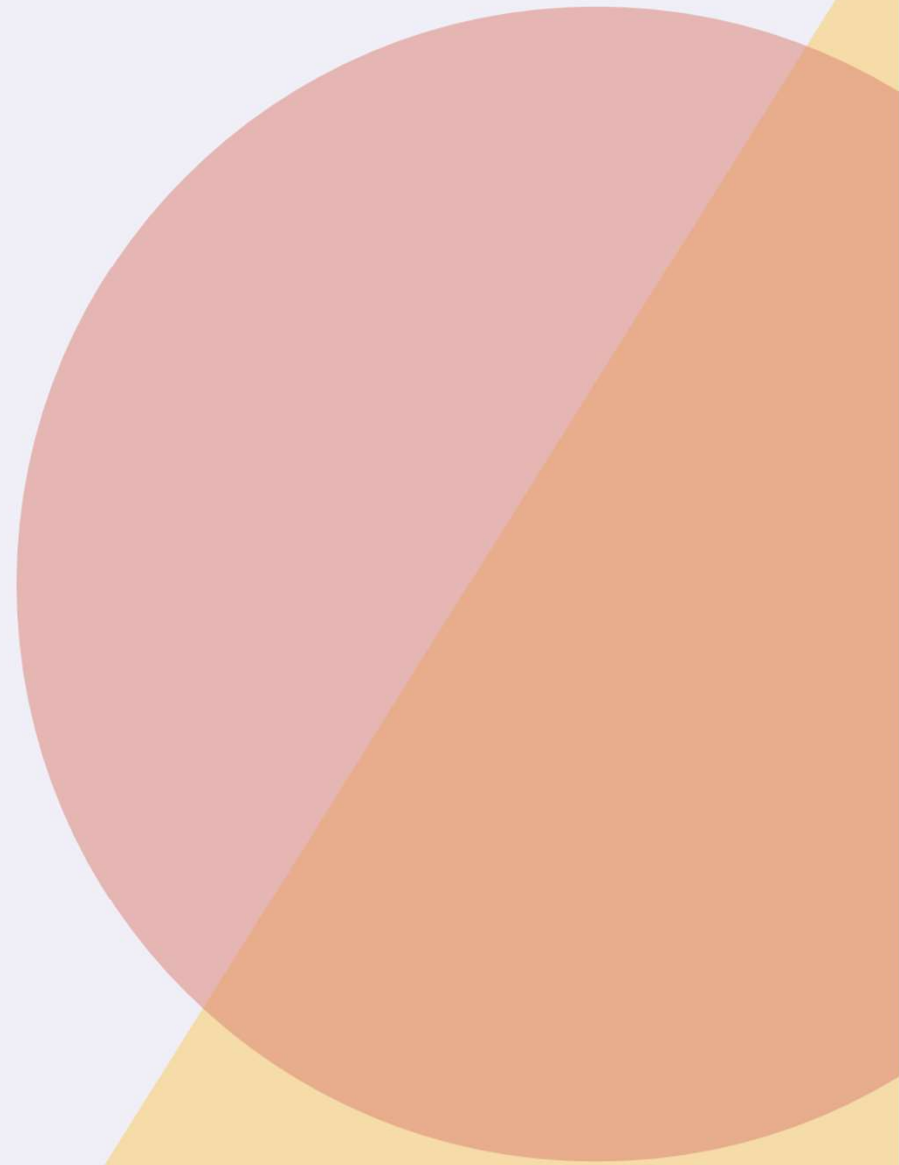
Life assured is
Director (Mr A)

Insurable interest - not required – Capital redemption option

Jones family trust
(trustees are owners)

No life or lives
assured

Accessing tax free
'allowances' with an
offshore bond



The order of income tax

Onshore Bond gains

tax 4th

Dividends

tax 3rd

Savings income (including offshore bond gains)

tax 2nd

Earnings, pensions, trading profits & rental income

tax 1st

Tax free offshore bond gains

Use tax free savings allowances

PSA	£1,000	No tax
Starting Rate	£5,000	No tax
Personal Allowance	£12,570	No tax

Total £18,750

Bond tax in 3 Steps

- 1) Wait for a chargeable event
- 2) Calculate the gain arising
- 3) Attribute to a chargeable person



Bond chargeable events



D

Death of a life assured giving rise to benefits



A

Assignment for money or money's worth



M

Maturity (e.g. a Capital Redemption Bond)



E

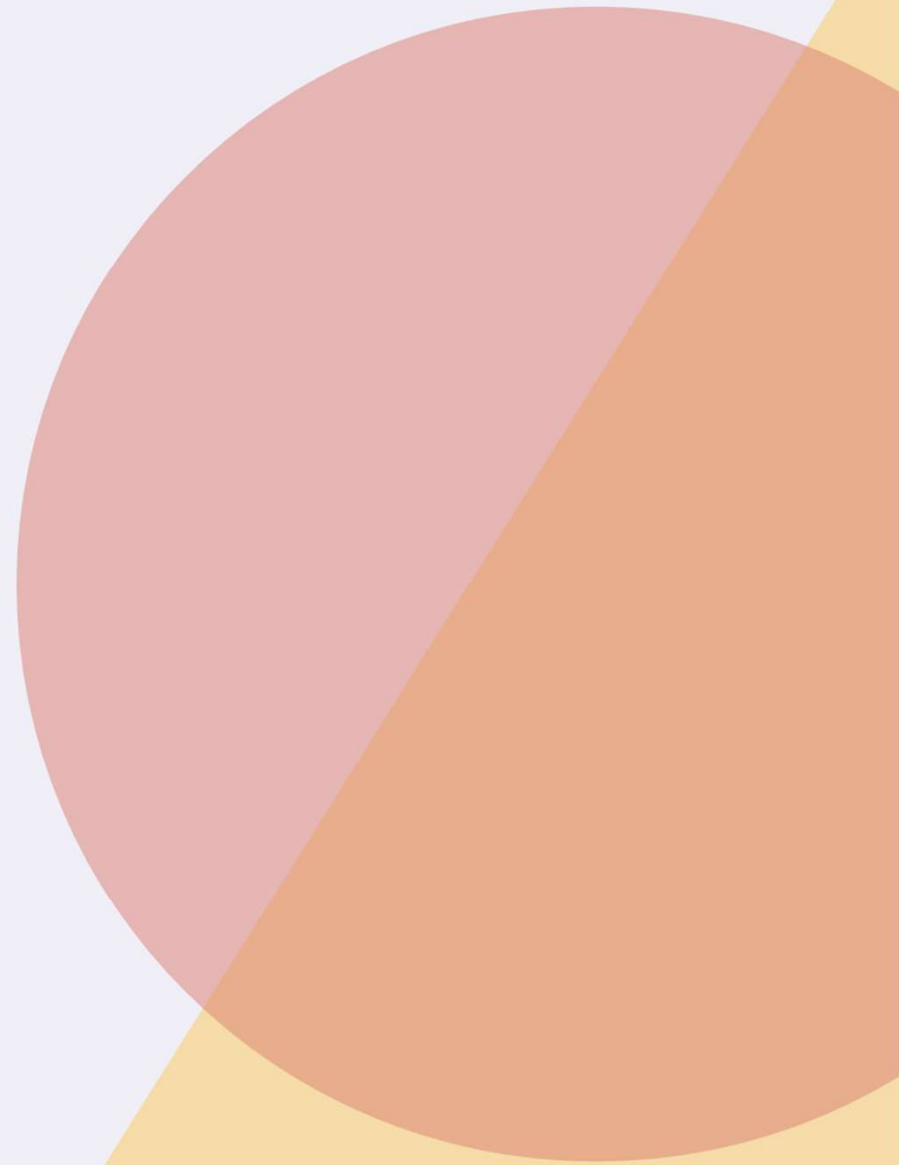
Excess part surrenders above 5% limits



S

Surrender in full

Putting the client in
control



Controlling Bond chargeable events



D

No C.E. if
surviving life
assured



A

No C.E. if gifted
assignment



M

Life bonds don't
typically mature



E

No C.E if stick
to 5% limits



S

Choose tax
year
carefully

Part surrenders – the 5% rule

Invest £ 01 Jan 2021	Insurance year	Unused 5% allowance B/F £	5% allowance current year £	Part surrender in current year £	Gain £	Unused 5% allowance C/F £
100,000	01/01/21 to 31/12/21	N/A	5,000	Nil	Nil	5,000
	01/01/22 to 31/12/22	5,000	5,000	(9,000)	Nil	1,000
	01/01/23 to 31/12/23	1,000	5,000	(8,000)	2,000	Nil

Gain of £2,000 arises at 31/12/23 and falls in tax year 2023/24

The 5% annual limit

Not a tax free amount. All amounts withdrawn have to be taken into account in the calculation of any gain made when the policy ends



The five main triggers reordered - Why?



Excess part
surrenders above
5% limits



Death of a life
assured giving rise
to benefits



Assignment for
money or money's
worth

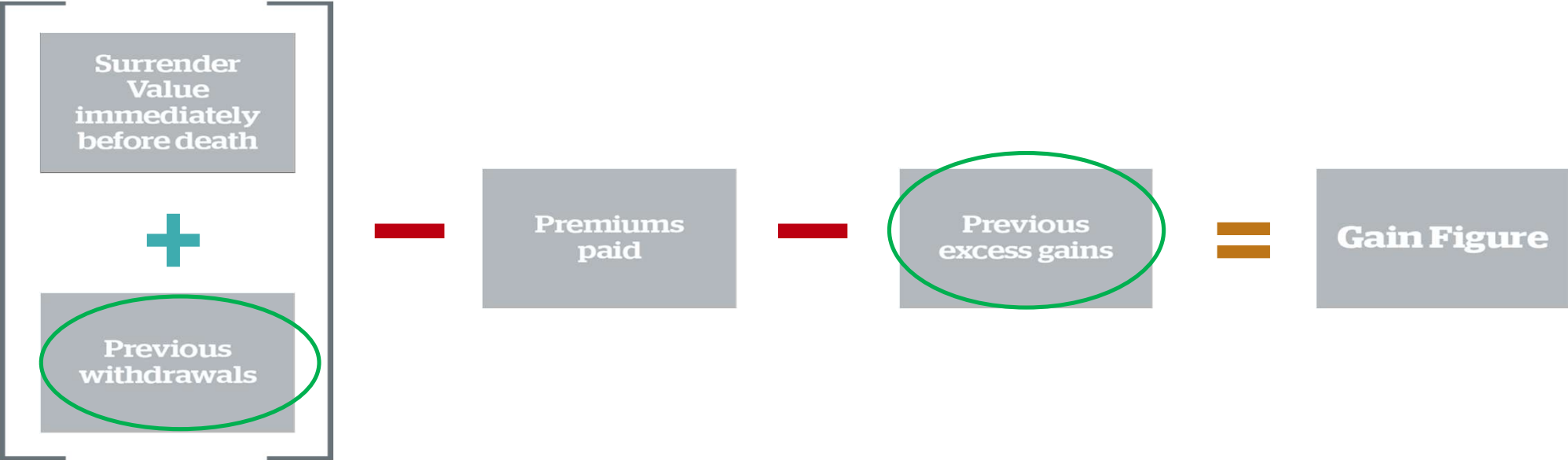


Maturity
(e.g. a Capital
Redemption Bond)



Surrender
in full

Final Gain calculation – part surrenders are tax deferred & not tax free



The 5% allowance

Beware large part surrenders as these can have unintended tax consequences.



Beware large part surrender gains

Invest £	Insurance year	Unused 5% allowance B/F £	5% allowance current year £	Part surrender in current year £	Gain £	Unused 5% allowance C/F £
200,000	01/02/23 to 31/01/24	N/A	10,000	(150,000)	140,000	Nil

Chargeable event gain of £140,000 arises at 31/01/24 (2023/24)

There are two potential ways of retrospectively 'correcting' this.

Joost Lobler – investment of \$1,406,000

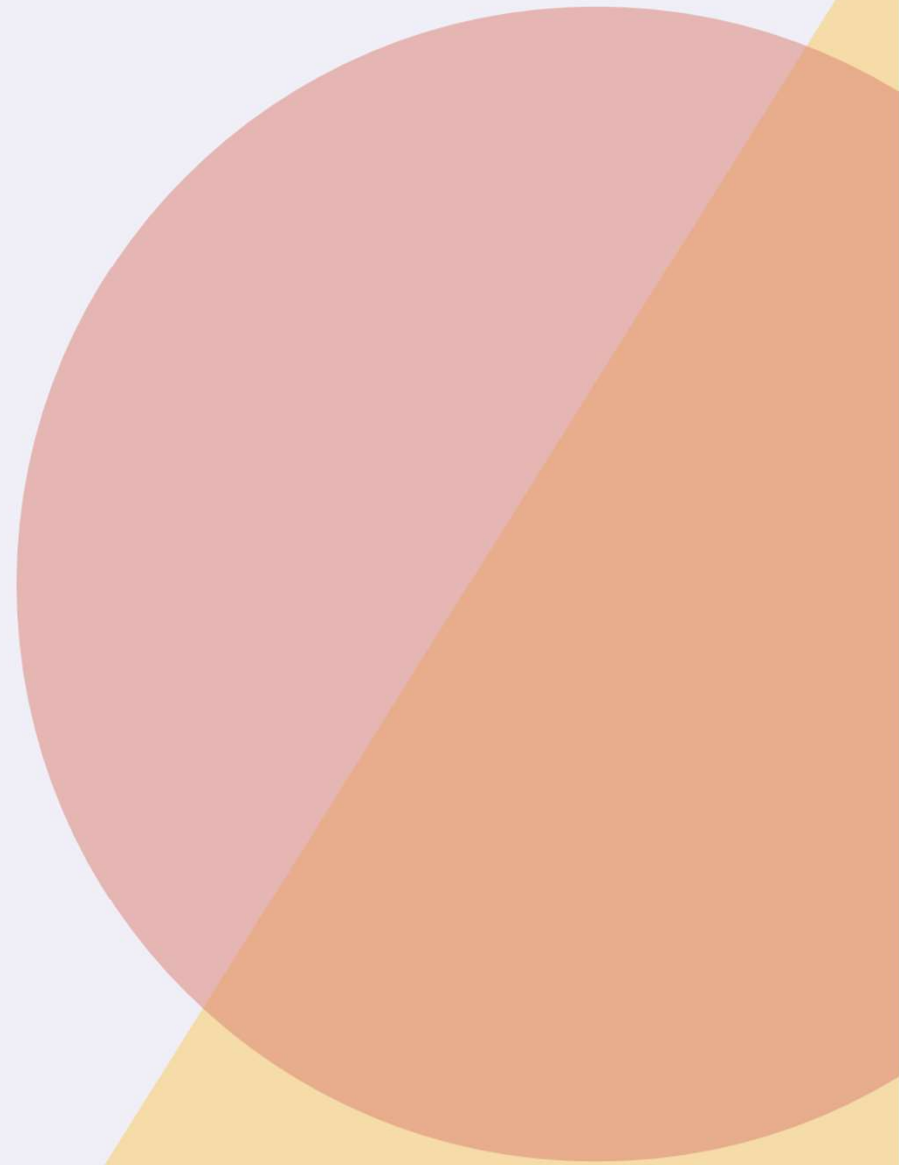
	5% allowance \$	Part Surrenders \$	Gain at end of insurance year \$
Insurance year 1	70,300	746,485	676,185
Insurance year 2	70,300	690,171	<u>619,871</u>
			<u>1,296,056</u>
Approximate tax liability			<u>560,000</u>

Joost Lobler – the fallout

+	—
×	==

- Economic gain?
- Premiums(s) paid?
- Tax due if not recalculated?
- Those liable need to apply & explain!
- 4 years from end of tax year
- Insurance company not involved

Withdrawal flexibility



Full surrender of individual segments v withdrawal across all segments



Year 3
Value £110,000.
Withdrawal required £33,000

“Full” – segment surrender

Segment value £11,000
Original Value £10,000
Gain per segment £1,000

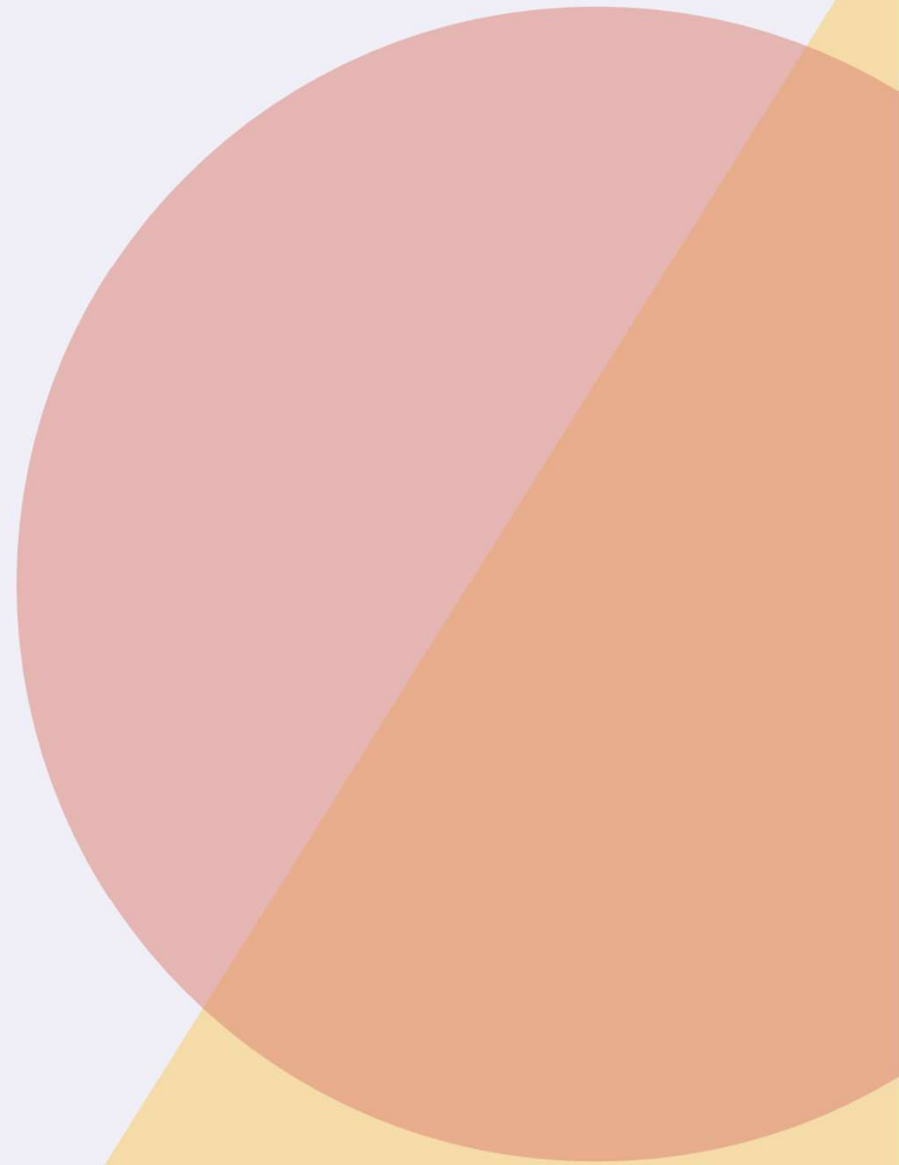
3 segments = £3,000 gain

“Partial” – across segments

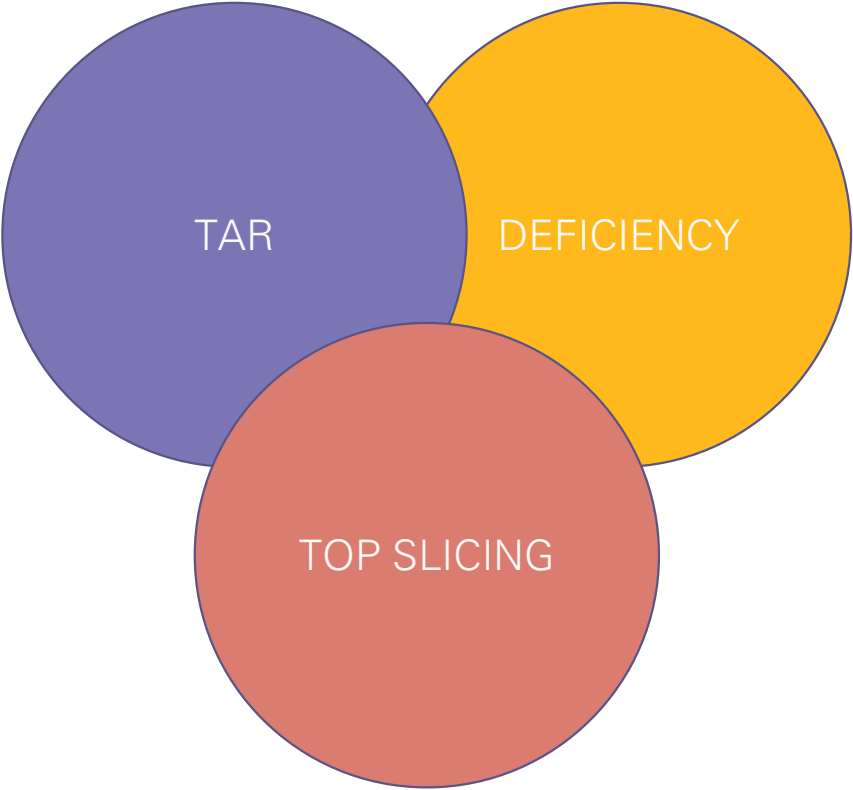
Withdrawal value £33,000
Tax deferred available £15,000

£18,000 gain

The three reliefs



That's a relief



Time Apportionment Relief

5 things **you need** to know

1

Onshore and offshore

2

The residence history of the person liable to tax

3

Reduce the gain by A/B

4

Statutory residence test

5

Why it's beneficial

Deficiency Relief

5 things **you need** to know

1

Losses are just
nil gains

2

The importance
of S539 ITTOIA
2005

3

How deficiency
relief arises

4

How deficiency
relief is given

5

An example

Calculating deficiency relief



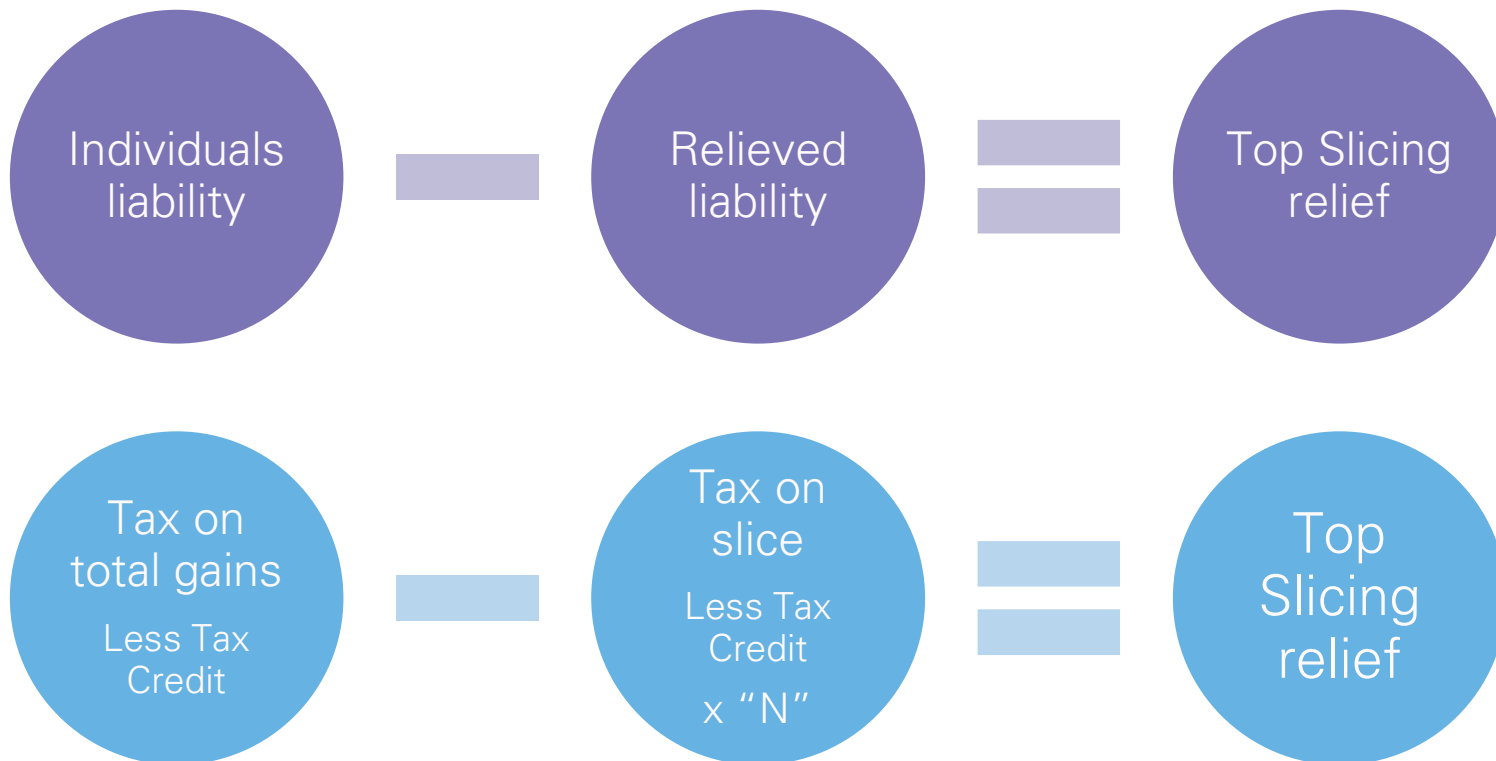
Jo invested £20,000 in a bond and in the 2nd insurance year an £8,000 part surrender triggered a £6,000 gain. A few years later she encashed for £10,000

Final surrender calc $£10,000 + £8,000 - £20,000 - £6,000 = (£8,000)$

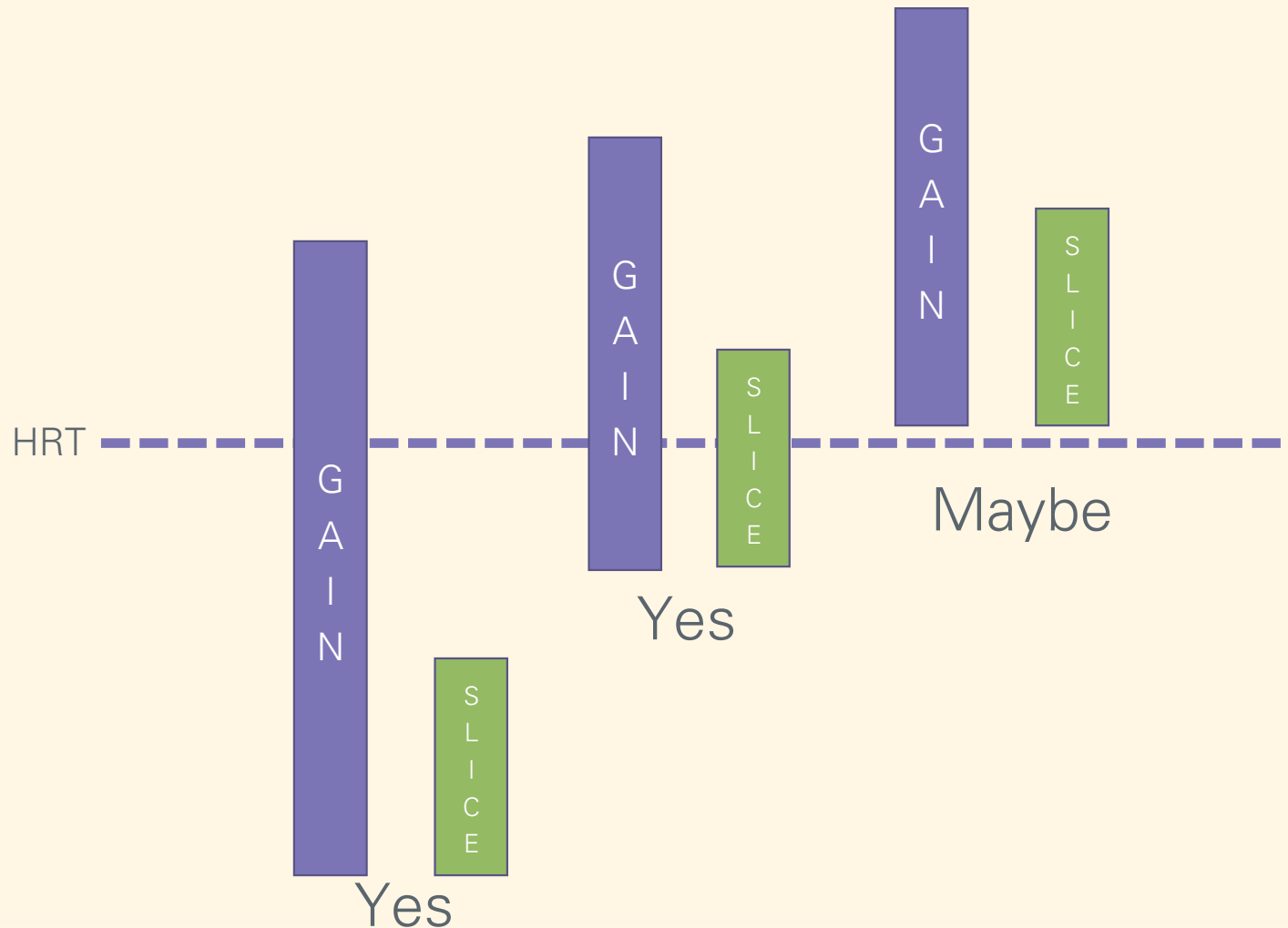
Deficiency relief restricted to £6,000 (i.e. total prior gain)

In tax year of full surrender, Jo only has employment income which breaches the higher rate threshold by £3,300. That £3,300 can be relieved by deficiency relief.

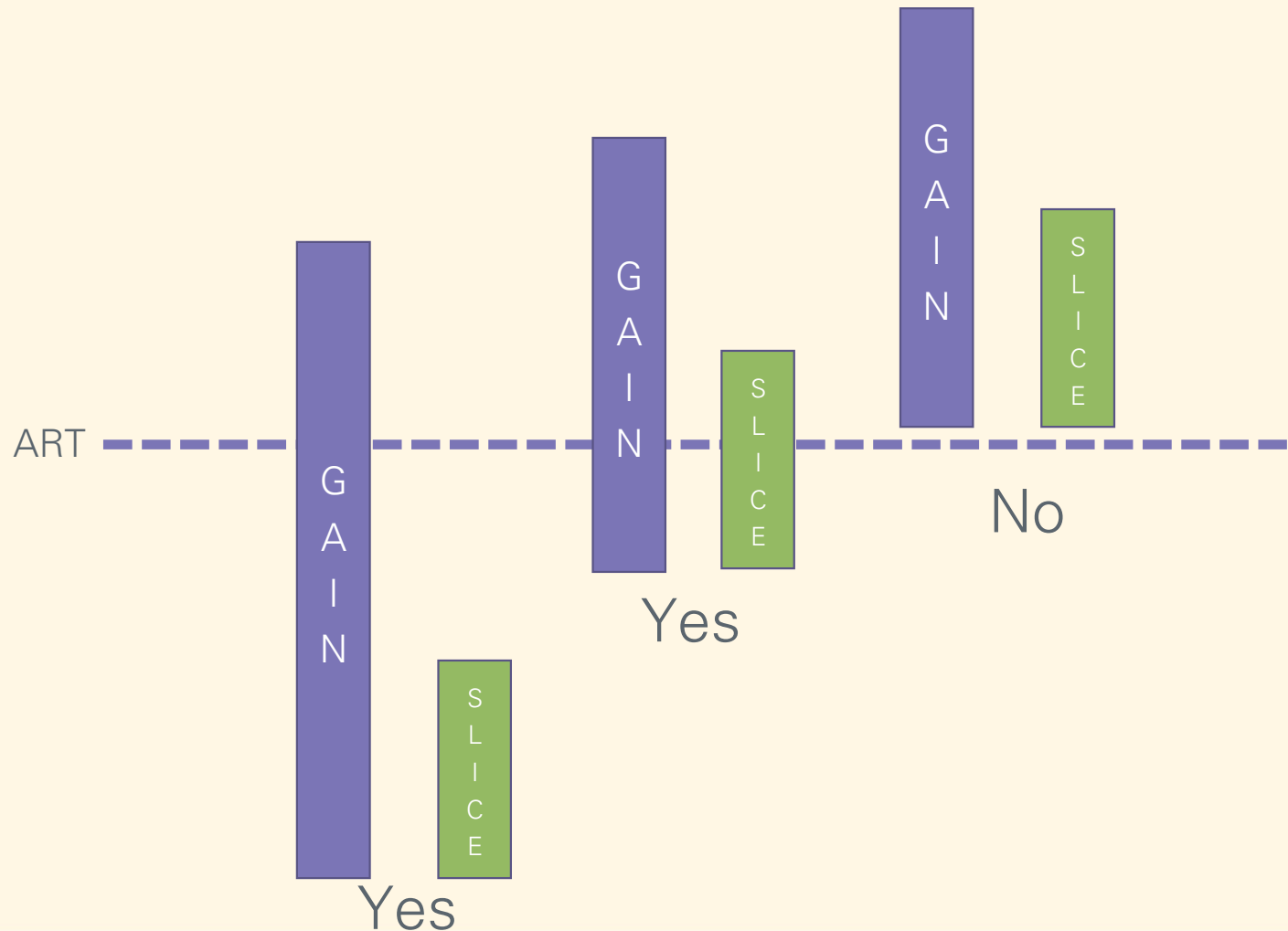
Top slicing – 3 easy steps



Tax reduced? – Higher rate threshold



Tax reduced? – Additional rate threshold





Tax Wrapper Comparison Tool

Tax Relief Modeller

Bond Gain Tool

Tax Relief Modeller Tool

built by M&G

ABOUT YOUR CLIENT

What is the client's age?	<input type="text" value="Under 75"/>
Scottish Tax Payer?	<input type="text" value="No"/>
Number of Children	<input type="text"/>
Gift Aid (Gross amt)	<input type="text"/>

CHARGEABLE EVENTS - BOND GAINS

Onshore Gain 1	<input type="text" value="250,000"/>	Years Gain 1 (N)	<input type="text" value="37"/>	Slice 1	<input type="text" value="6,757"/>
Onshore Gain 2	<input type="text"/>	Years Gain 2 (N)	<input type="text"/>	Slice 2	<input type="text"/>
Onshore Gain 3	<input type="text"/>	Years Gain 3 (N)	<input type="text"/>	Slice 3	<input type="text"/>
Onshore Gain 4	<input type="text"/>	Years Gain 4 (N)	<input type="text"/>	Slice 4	<input type="text"/>
Offshore Gain 1	<input type="text"/>	Years Gain 1 (N)	<input type="text"/>	Slice 1	<input type="text"/>
Offshore Gain 2	<input type="text"/>	Years Gain 2 (N)	<input type="text"/>	Slice 2	<input type="text"/>
Offshore Gain 3	<input type="text"/>	Years Gain 3 (N)	<input type="text"/>	Slice 3	<input type="text"/>
Offshore Gain 4	<input type="text"/>	Years Gain 4 (N)	<input type="text"/>	Slice 4	<input type="text"/>

INCOME SOURCES

Employment Income	<input type="text"/>
Benefits in Kind	<input type="text"/>
Taxable Self Employed Profits	<input type="text"/>
UFPLS (taxable element)	<input type="text"/>
Drawdown / Annuity Income	<input type="text"/>
State Pension Income	<input type="text" value="8,000"/>
Purchased Life Annuity Income	<input type="text"/>

Gross Savings Interest	<input type="text"/>
Dividends	<input type="text"/>
Taxable Capital Gains (10%/20%)	<input type="text"/>
Taxable Capital Gains (18%/28%)	<input type="text"/>
Taxable Redundancy Payment	<input type="text"/>
Rental Income - Relevant	<input type="text"/>
Rental Income - Not relevant	<input type="text" value="38,000"/>

EXISTING PENSION CONTRIBUTIONS

Relief at Source (Net Amount)	<input type="text"/>
Contributions paid gross	<input type="text"/>

NEW PENSION CONTRIBUTIONS

Relief at Source (Net Amount)	<input type="text" value="2,880"/>
Contributions paid gross	<input type="text"/>

R
E
S
E
T

BEFORE NEW CONTRIBUTIONS

"Total Income"	£296,000
Adjusted Net Income	£296,000
Personal Allowance	£0
Personal Savings Allowance	£0
Child Benefit Charge	£0
Capital Gains Tax	£0
Tax Liability	£29,262
Bond Gains Summary	
Tax on gains	£107,300
Onshore Tax Credit	£50,000
Top slicing relief	£38,898
Liability	£18,402
"Bank Balance"	£266,738

AFTER NEW CONTRIBUTIONS

"Total Income"	£296,000
Adjusted Net Income	£292,400
Personal Allowance	£0
Personal Savings Allowance	£0
Child Benefit Charge	£0
Capital Gains Tax	£0
Tax Liability	£10,140
Bond Gains Summary	
Tax on gains	£107,120
Onshore Tax Credit	£50,000
Top slicing relief	£57,120
Liability	£0
"Bank Balance"	£282,980

DIFFERENCE

	£0
	-£3,600
	£0
	£0
	£0
	£0
	-£19,122
	£180
	£0
	£18,222
	-£18,402
	£16,242

PENSION SUMMARY

Relevant Earnings	£0
Contributions: Existing	£0
New	£3,600
Total	£3,600

**Effective Rate
of
Tax Relief**
(on new contributions)

551.17%

Please navigate between workings and inputs using the tabs at the bottom of the sheet.

Tax Wrapper Comparison Tool

built by M&G

Tax Year 2022/23

Invested Amount

Year of encashment (5 to 10 only)

Reset

Investment Yields

Savings income	<input type="text" value="3.00%"/>
Dividend Return	<input type="text" value="3.00%"/>
Capital Gain	<input type="text" value="3.00%"/>
Additional Cost for Bond Wrapper	<input type="text" value="0.25%"/>

Onshore Bond
Internal Tax Rate
13.33%

Existing income

	Existing income	Increase assumption per annum
Non Savings Non Dividend	<input type="text" value="£60,000"/>	<input type="text" value="0.00%"/>
Savings	<input type="text" value="£0"/>	<input type="text" value="0.00%"/>
Dividend	<input type="text" value="£0"/>	<input type="text" value="0.00%"/>

Expected Income year of encashment

Non Savings Non Dividend	<input type="text" value="£20,000"/>
Savings	<input type="text" value="£0"/>
Dividend	<input type="text" value="£0"/>

Taxation over Term

	Collectives	Onshore	Offshore
Savings Income			
Amount	£82,731	£85,005	£89,980
Tax	£28,897	£17,001	£0
Dividend Income			
Amount	£82,731	£85,005	£89,980
Tax	£23,447	£0	£0
Capital Gain			
Amount	£33,000	£85,005	£89,980
Tax	N/A	£17,001	£0

Encashment Values

	Collectives	Onshore	Offshore
Surrender Value	£395,849	£413,377	£461,768
Gain (Cumulative)	£52,731	£213,377	£261,768
Slice	N/A	£21,338	£26,177
Tax payable	£9,114	£2,514	£54,868
Net return	£386,735	£410,863	£406,901

Key Assumptions

Cells with red tags contain further information

The tool runs in tax years from 6 April to 5 April inclusive.

The CGT allowance in year one is £6,000, thereafter this is £3,000.

The Dividend Nil Rate in year one is £1,000, thereafter this is £500.

The CGT annual exempt amount is used each year (bed and breakfast rules avoided).

Net investment income is reinvested.

UK rates of income tax apply.

Available Bands and Allowances in year of encashment (prior to investments being surrendered)

	Collectives	Onshore	Offshore
Personal Allowance	N/A	£0	£0
Starter Rate for Savings	N/A	£0	£0
Personal Savings Allowance	N/A	£1,000	£1,000
Basic Rate	£8,320	£30,270	£30,270
Higher Rate	N/A	£87,440	£87,440
CGT Allowance	£3,000	N/A	N/A

Back or never away?

Bob earns £60,000 a year

He uses his ISA allowance each year.

He has £250,000 to invest.

His adviser expects to be:

- 2.5% gain
- 2.5% dividend
- 2.5% interest

He will likely access the money in 10 yrs when he has expected pension income only of £20,000.

AEA is used annually.

A bond is 0.25% a year more expensive

Dividend Allowance £2,000 CGT AEA £12,300

Encashment Values			
	Collectives	Onshore	Offshore
Surrender Value	£448,978	£457,683	£502,520
Gain (Cumulative)	£10,503	£207,683	£252,520
Slice	N/A	£20,768	£25,252
Tax payable	£0	£2,514	£53,018
Net return	£448,978	£455,169	£449,502

Including Dividend and CGT reductions

Encashment Values			
	Collectives	Onshore	Offshore
Surrender Value	£443,002	£457,683	£502,520
Gain (Cumulative)	£51,594	£207,683	£252,520
Slice	N/A	£20,768	£25,252
Tax payable	£8,765	£2,514	£53,018
Net return	£434,237	£455,169	£449,502

Why bonds

Return expected to be income driven (especially dividends)

Those who can manipulate income in year of access

Higher rate tax payers who expect to be basic on access

Receive "income" with no immediate tax impact

Expectation of lifetime gifting

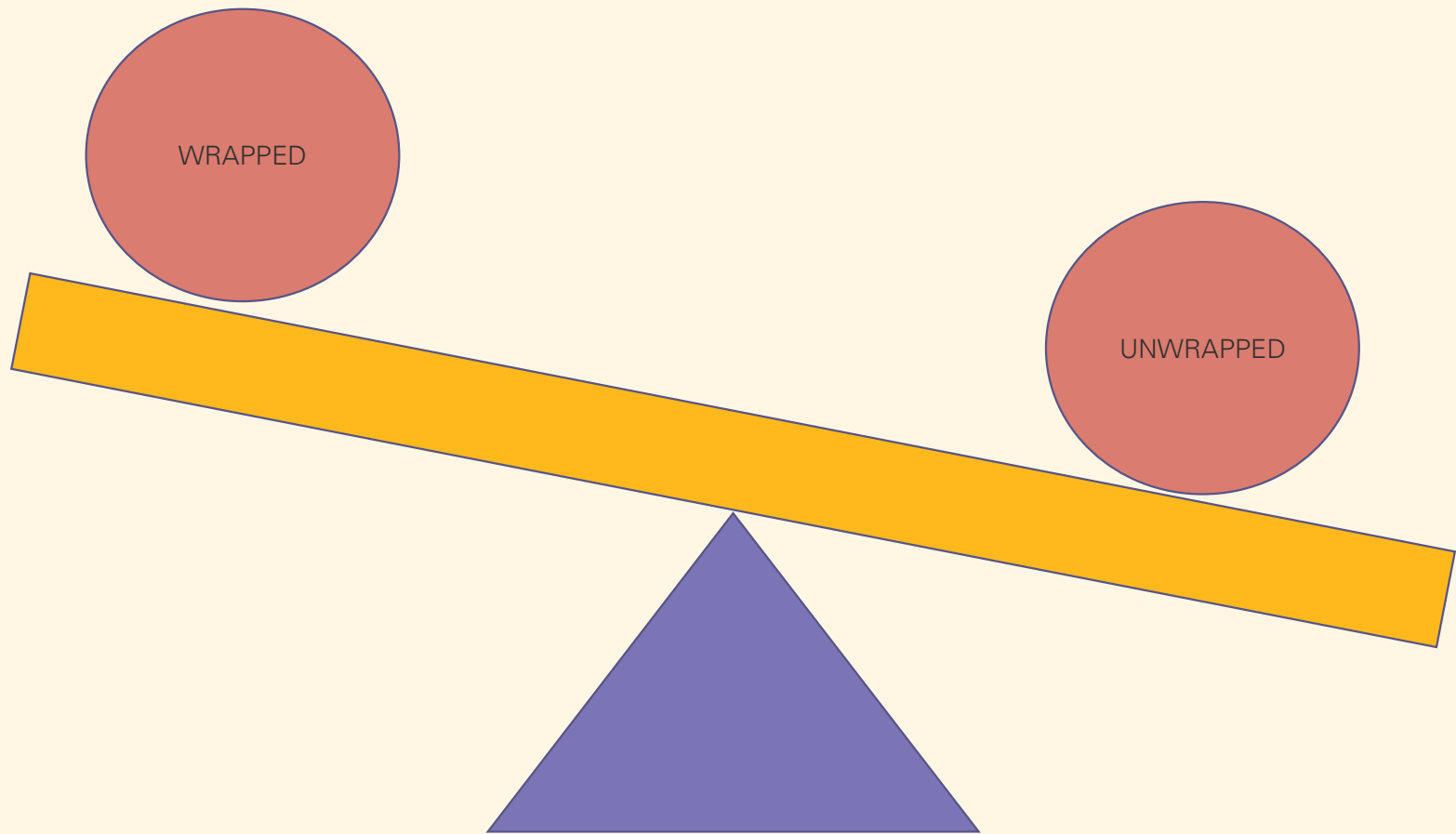
Access savings allowances with equity funds

Larger / Active Portfolios

Those looking for simplicity / low admin

Reliefs and fund availability

The future



Learning Objectives

By the end of this session, you will be able to:

Describe the impact of the changing tax landscape on investment advice

Describe the taxation of insurance bonds

Identify clients who would benefit from using insurance bond wrappers

Support



Articles



Videos



Tools &
Calculators



Ask the Techs
Usual Contact
LinkedIn
My View

Thanks for your time

Get in touch with your usual contact if you need further help.





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